United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

ORIGINAL

75-1004

To be argued by
CHARLES A. STILLMAN

United States Court of Appeals
FOR THE SECOND CIRCUIT

Docket No. 75-1004

UNITED STATES OF AMERICA,
Appellee,

against

ANTHONY M. NATELLI and JOSEPH SCANSAROLI,
Defendants-Appellants.

APPEAL FROM JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK
(D.C. Crim. No. 74 Cr. 43)

BRIEF ON BEHALF OF APPELLANT JOSEPH SCANSAROLI

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Statement of Issues Presented for Review

1. Whether the evidence—characterized by the trial court as presenting a "close question"—was sufficient to support the conviction of Joseph Scansaroli.

2. Whether Joseph Scansaroli was deprived of a fair trial as a result of the following errors:*

* The brief submitted on behalf of appellant Anthony Natelli challenges other rulings of the trial court, and demonstrates the errors in certain critical aspects of the court's charge. All of those points are applicable to Scansaroli and we adopt them.

a. the improper admission of hearsay testimony;

b. the improper admission of so-called "victim" testimony;

c. the trial court's refusal to define "aiding and abetting" in its charge to the jury.

Preliminary Statement

Defendant-appellant Joseph Scansaroli appeals from a judgment of conviction entered on December 27, 1974, by the United States District Court for the Southern District of New York (Tyler, *J.*).

The judgment of the District Court (A.333):*

(a) upon a jury's verdict, convicted Scansaroli on the single count of the indictment in which he was named; and

(b) sentenced Scansaroli to a term of one year in prison, suspended execution of all but ten days, placed Scansaroli on unsupervised probation for the balance, and fined him $2,500.

Scansaroli and the Indictment

The indictment in this case contained fourteen counts, naming seven defendants and four unindicted co-conspirators (A.12).

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* References are to pages in the Appendix. The Appendix consists of four volumes. Volume I contains the pertinent pre-trial and post-trial proceedings (references to pages in this volume are designated "A"). Volumes II-IV contain the transcript of the trial (references to pages in these volumes are designated "T"). The pertinent exhibits are contained in a separate volume. References to exhibits are cited as follows: "GX" refers to government's exhibits; "NX" refers to Natelli's exhibits; "SX" refers to Scansaroli's exhibits; and "Ct. X" refers to the Court's exhibits (references to pages in this volume are designated "E").

Scansaroli was named a defendant in only one count, Count II. That count charged Scansaroli and appellant Natelli, an employee and partner, respectively, of Peat, Marwick, Mitchell & Co. ("PMM"), together with four of the five other defendants, with a substantive violation of 15 U.S.C. § 78ff. Count II alleged that the named defendants had made, or aided and abetted the making of (18 U.S.C. § 2), false and misleading statements in a September 27, 1969 proxy statement issued and filed by National Student Marketing Corporation ("NSMC").

The remaining thirteen counts charged certain NSMC officers and executives with conspiracy and various substantive violations of the federal securities laws. Scansaroli was not named in any of these counts.

Aside from Natelli and Scansaroli, the defendants named in the indictment were:

Cortes W. Randell—president and chief executive officer of NSMC.

Robert C. Bushnell—an officer and "account executive" of NSMC.

Dennis M. Kelly—another officer and "account executive" of NSMC.

John G. Davies—principal in-house counsel to NSMC.

Bernard Kurek—originally controller and later vice president and treasurer of NSMC.

Pre-Trial Proceedings

Although there were several pre-trial motions, it is only necessary for the purposes of this appeal to refer to those dealing with venue and the admissibility of polygraph examinations. These motions are discussed in Points IV and VI of the brief on behalf of Natelli and we adopt them.

Defendants Randell, Bushnell, Kelly and Kurek entered pleas of guilty to some of the counts in which they were named: Randell (Counts 1, 2, 8 and 11) was sentenced to eighteen months' imprisonment and a fine of $40,000 (A.314-15, 322); Bushnell (Count 1) received a six-month suspended sentence and was placed on probation for two years (A.324-25); Kelly (Count 1) was sentenced to ten months' imprisonment and a fine of $10,000 (A.319-20); and Kurek, who was later to become the government's principal trial witness, pleaded guilty to Count 2 and received a suspended sentence (A.331). The trial of Davies commenced on March 5, 1975 and terminated upon Davies' plea of guilty.

Trial Proceedings

The trial of the single charge against Natelli and Scansaroli commenced on October 21, 1974 before Judge Tyler and a jury. At the conclusion of the government's case and again at the conclusion of the entire case, the court denied all defense motions for judgment of acquittal (T.1318-22, 1334-38, 2129-36).

The charge of the trial court and the deliberations of the jury are discussed in the brief on behalf of Natelli which addresses certain errors in the charge. We discuss below (Point IV) the failure of the trial court to define aiding and abetting.

The case was submitted to the jury on November 13, 1974. The next afternoon, the jury, after having announced a deadlock, returned verdicts of guilty.

Post-Trial Proceedings

Subsequent to trial, Scansaroli moved for a judgment of acquittal or for a new trial. Judge Tyler denied this motion as well, on December 20, 1974 (A.248).

Statement of the Evidence as to Joseph Scansaroli

Introduction

In this case, the words and deeds of Joseph Scansaroli were seen only in the inescapable shadow of the repeated assertions of deception practiced by the principal officers of National Student Marketing Corporation. But the government did not suggest, in the indictment or elsewhere, that Scansaroli conspired with these deceivers, that he was a party to their scheme, or that he profited from their fraudulent enterprise in any way.

The single count of the indictment naming Scansaroli charged that he and Natelli participated in the preparation of a 270-page NSMC proxy statement assertedly containing two false and misleading elements: An explanatory footnote to NSMC's audited financial statements for the fiscal year ended August 31, 1968, and a portion of the unaudited statement of NSMC's earnings for the nine-month period ended May 31, 1969.

It is the principal burden of this brief to focus clearly on the particulars of this charge; to sift through the testimony and mountains of documents; to scrutinize the words and deeds of Joseph Scansaroli as adduced at trial; and, finally, to demonstrate that when viewed as they should be, in the human context in which they occurred, those words and deeds were legally insufficient evidence from which a reasonable jury could fairly conclude that Joseph Scansaroli knowingly and wilfully participated in any criminal conduct.

To that end, the statement of facts set forth below will center on Scansaroli's participation—or lack of it—in the preparation of the footnote and the unaudited earnings statement described in Count II and the context in which his words and deeds occurred. A more detailed descrip-

tion of PMM's relationship with NSMC can be found in the statement of facts in the brief on behalf of Natelli, to which the Court's attention is respectfully referred.

A. The General Background.

In August 1968, Joseph Scansaroli was a 32-year old certified public accountant who had risen, in five years, from junior accountant to senior accountant to supervisor with Peat, Marwick, Mitchell & Co. (T.1480-81). In that month, PMM was introduced to National Student Marketing Corporation, a young public company engaged in the promotion of nationally-known products to a market comprised of high school and college students (T.1484). When NSMC engaged PMM as its independent auditors (replacing Arthur Andersen & Co.), Natelli became the audit partner and Scansaroli the supervisor. Two younger accountants, John Johnston and Douglas Oberlander were also assigned to the NSMC engagement (T.1488).

1. *The 1968 Audit.*

The first major task to be performed by these four PMM accountants was the audit of NSMC's financial statements for the fiscal year ended August 31, 1968, which, through November 1968, when the audit was completed, occupied more than 600 hours of their time (T.1488-89). It is important to note that *none* of the work done by Natelli, Scansaroli, Johnston and Oberlander during the course of their work on the 1968 audit was even mentioned in the indictment and that none of it has ever been the subject of any criminal charges. Later events, however, gave significance to two of the many accounting judgments that were made. Neither of these two judgments was made by Scansaroli (T.1839-42).*

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* By pointing out that these two acounting judgments were not made by Scansaroli, we do not mean to imply in any way that any criminal decision was made by anyone on behalf of PMM.

2. *Confirmation of Commitments.*

An important segment of NSMC's business was the generation of commitments by NSMC customers to utilize NSMC marketing services for the promotion of their products (T.336). Naturally, one of the tasks confronting the auditors was the confirmation of these commitments.

NSMC's president, Randell, explained that NSMC had not obtained written commitments from its clients—that given the nature of advertising people, Randell would prefer that PMM not confirm the commitments in writing, but rather seek alternative means to satisfy itself as to the validity of the commitments (T.1499). Natelli decided that together with other audit evidence, oral confirmation would suffice (T.1839). Accordingly, he instructed Scansaroli to meet with NSMC's account executives in NSMC's New York office and to discuss with them the commitments they had received. Natelli also instructed Scansaroli to review any documents or correspondence the account executives had with respect to these commitments and to test the existence of these commitments by making telephone calls at random to the clients involved (T.1839-40).

As instructed, Scansaroli went to New York and met with the account executives; he reviewed the documentation in their files; and he telephoned representatives of the major clients who had given oral commitments to NSMC's account executives (T.1501).* Scansaroli returned to Washington where he made additional telephone calls (T.1501), and ultimately reported to Natelli that he was satisfied that the commitments could be accrued by the company (T.1627).

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* Scansaroli's work product was bound up by him in what has been described as the Special Sales Binder (GX 3). The contents of this binder and the work that went into it were vigorously attacked by the government as slipshod and grossly negligent (T.2276-77, A.177-78). But no one has ever claimed that Scansaroli was corruptly motivated in doing this work—indeed, the trial court found the opposite to be true (A.263).

3. *Recognition of Income.*

Once there appeared to be adequate audit evidence of the commitments, PMM had to determine the accounting method by which the commitments—also known as contracts-in-progress—would be reflected in NSMC's financial statements. Typically, the commitments involved the planning and preparation of marketing programs which would then be effectuated in the coming academic year (T.336-37, 1494-95).

Because much of NSMC's work—principally the creation and development of marketing programs for its customers—on the commitments had been performed prior to August 31, 1968, the date of the financial statements, NSMC officials took the position that the income should be accrued, even though payment by the client was not expected until implementation of the program in the following months. Natelli decided that NSMC could properly recognize that portion of the expected revenue represented by the ratio of the creative time actually expended on a particular program to the total time expected through that program's completion. In this way, revenues and earnings would be reported by NSMC in the accounting periods in which the work was performed, without regard to subsequent payment dates. Thus the company's 1968 financial statement reflected the accrual of this income—described as "Unbilled receivables and accrued costs and estimated earnings on contracts in progress"—and an explanation of the theory was supplied by an appropriate footnote (GX5, E.55-6) (Natelli Brief, pp. 12-13).

B. The September 1969 Proxy Statement.

1. *May 1969.*

After completion of the 1968 audit, except for a single meeting he attended in December 1968, at which Natelli informed NSMC officials that only written commitments

would be acceptable to PMM in the future, that account executive time logs would be mandatory and that improved control should be maintained on the status of the contracts (T.1845-50), Scansaroli had virtually no contact with NSMC until the spring of 1969 (T.1522-23).

In late April or early May 1969, Natelli and Scansaroli were informed that NSMC proposed to issue a proxy statement soliciting shareholder approval of an increase in NSMC's authorized capital stock which would permit it to acquire other companies engaged in related businesses (T.250, 649). The proxy statement was to include, among much other information, NSMC's previously issued audited financial statements, as restated for poolings of interests, for the fiscal year ended August 31, 1968 and unaudited financial statements for the six-month period ended February 28, 1969.

After the work had begun, Natelli learned from Davies, NSMC's inside counsel, and subsequently informed Scansaroli, that certain of the contracts-in-progress that had been included in NSMC's 1968 revenues and earnings and totalling approximately $750,000, had been determined by NSMC's management to have been non-existent (T.370-73): Contracts between NSMC and Clairol, Ban, Chesebrough and Listerine been fictitiously reported by account executive Ronald Michaels,* and were thus considered by NSMC never to have existed in the first place. These facts had been learned by NSMC only after Michaels had been discharged for engaging in other dishonest activities (T.1853-54).

John Buck, then NSMC's controller, or Kurek asked Natelli and Scansaroli for their advice as to an appropriate way to enter on the company's books the write-off of the Michaels contracts and the related costs which had been

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* Michaels was named in the indictment as a co-conspirator, but not a defendant.

accrued (T.635-36). Natelli assigned to Scansaroli the job of drafting proposed adjusting journal entries (T.1536-37).

At about the same time, a PMM tax specialist, Carol Raimondo, was reviewing NSMC's 1968 tax return, which was due to be filed on May 15, 1969. As with many public corporations, NSMC's "book" (financial statement) accounting differed in some respects from its tax accounting, principally due to certain "timing differences." Because of these differences, NSMC's financial statements reflected, in the form of a "deferred tax liability," taxes which NSMC would be required to pay in future periods. In 1968 NSMC had increased its deferred tax liability by approximately $190,000 (T.1392).

In reviewing NSMC's 1968 tax return, however, Mrs. Raimondo, in a contemporaneous memorandum, noted that for various reasons, including these same timing differences (reducing NSMC's revenue and increasing its expenses for tax purposes), NSMC showed a loss for the year on its tax return (NX P, E.496). Mrs. Raimondo advised Scansaroli, who as she testified, relied on her expertise as a tax specialist (T.1389), that because NSMC had sustained this tax "loss" for the year, as it had in the prior year, the loss would create a "carry-forward" which could be used to offset future income, thereby reducing any taxes due in future periods. Mrs. Raimondo's conclusions, she told Scansaroli, were that NSMC had no need to reflect any deferred tax liability on its financial statements (T.1386-87), that the provision of $190,000 for this purpose had thus been made in error (T.1389-90), and that the deferred tax provision should be eliminated (T.1390), which would have the effect of an increase in 1968 net earnings by that amount.

Mrs. Raimondo discussed her reasoning and her conclusions with a PMM tax partner, Eugene Holloway, and with Natelli, who also discussed the matter with Holloway

(T.1859) as did Scansaroli (T.1541). The four agreed to eliminate the deferred tax provision in the August 31, 1968 financial statement.

Thus, at the time Scansaroli was preparing the proposed journal entries, he was working with the following: Four Michaels contracts as to which NSMC had reported for the year ended August 31, 1968, $748,762 in sales and $539,012 in expenses; and a deferred tax provision as of August 31, 1968, of approximately $190,000. As noted, one element of the equation would operate to reduce NSMC's income, and the other would increase NSMC's income. In preparing the proposed entry to adjust retroactively NSMC's financial statements as of August 31, 1968 (reflecting the decrease in earnings due to the write-off of the Michaels contracts and the increase in earnings caused by elimination of the deferred tax provision), Scansaroli dealt at first with only three of the four Michaels contracts (T.1543). The net result of writing off these three contracts (Clairol, Chesebrough and Ban) was a $188,750 decrease in earnings. In the same entry, rather than use the figure of $190,000, Scansaroli reduced the deferred tax elimination to the same $188,750, leaving the small balance as a "cushion" against future tax liability (T.1539-40). The net result of these entries was that there was no change at all in NSMC's net earnings for the year ended August 31, 1968, since those earnings were simultaneously increased and decreased by $188,750. The journal entry Scansaroli prepared in May, 1969 (GX 13, E.98) described exactly what he did: Write-off the Clairol, Chesebrough and Ban contracts and eliminate the deferred tax provision; and three months later, the 1968 financial statements for NSMC contained in the proxy statement reflected the sales figures as reduced by the Michaels contracts (T.1292-94; GX 25, E.212), and in a separate line in that statement reflected the elimination of the deferred tax provision by $188,750 (GX 25, E.167).

After Scansaroli prepared the proposed journal entries, he met with John Buck, the company controller, and dis-

cussed each component, including the Raimondo-suggested tax elimination (T.645-46). At a later date, Scansaroli, after discussion with Natelli, prepared an additional entry which was made by NSMC to reflect the write-off of the fourth Michaels contract (Listerine) (T.1542-43). The write-off of this contract involved $70,200 in revenues and $49,200 in accrued costs, or a net effect of $21,000 (GX 13, E.99).

In sum, then, the entries prepared by Scansaroli reduced NSMC's 1968 gross revenues by approximately $750,000, its expenses by approximately $540,000 and its 1968 net earnings by $21,000,* after giving effect to the elimination of the deferred tax provision.

During this same period, Natelli and Scansaroli were also informed that the company had concluded that an additional $212,000 in contracts-in-progress had been judged to be uncollectible because NSMC clients had changed their minds or had suffered budgeting problems requiring the cancellation of committed programs (T.635-39, 659). Buck prepared the necessary journal entry, writing off those commitments against current year's (1969) sales since in contrast to the non-existent Michaels "contracts," these commitments had become without value in the current year (T.639-40, 659).

2. *August 1969.*

a. The Footnote.

NSMC determined not to proceed, at least in May, with the proxy statement Natelli and Scansaroli had been work-

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* More than a year later, Scansaroli, then an employee of NSMC, in response to an SEC inquiry, determined that Mrs. Raimondo had apparently misread the applicable rules (APB Opinion No. 11) and that her conclusion had been in error (T.1690). Scansaroli reported his conclusion to Natelli and Kurek, who was then his superior. The matter was then brought to the attention of the SEC (T.1570-71).

ing on (T.1525). Scansaroli bound up and filed the workpapers containing the work he had done (T.1528).

In August, however, NSMC reactivated the proxy statement, and the same PMM team was assigned to the job (T.2051). This time, the proxy statement would include the unaudited financial statements for the nine-month period ended May 31, 1969.

Because NSMC had acquired several other companies since August 31, 1968, the financial data of which, under principles relating to the concept of "pooling of interests," were required to be combined retroactively with that of NSMC (T.1532-33), NSMC's consolidated financial statements for the year ended August 31, 1968, as they were to appear in the proxy statement, would bear no resemblance to those issued by NSMC in November 1968.

The NSMC sales and earnings figures for August 31, 1968 that were set forth in the proxy statement reflected the reductions that had been made as a result of the write-off of the Michaels contracts and listed an extraordinary credit for the elimination of the unnecessary deferred tax provision, which had the effect of increasing earnings by that amount.

NSMC's net sales had originally been reported as $4,989,446; after all adjustments, they would appear in the proxy statement as $11,541,895. Similarly, NSMC's net earnings had been reported as $388,031; as adjusted, they would appear as $773,152 (GX 25, E.169).

Following the procedure suggested by Accounting Principles Board opinion No. 10, Natelli drafted footnotes to show the effect of poolings upon the company's trend of earnings (T.1889; GX 17A, E.136). In the footnotes he included a line to show the losses on the Michaels contracts. When Natelli saw the footnotes in print, he realized that the difference attributable to the adjustments made in

May seemed insignificant when viewed against the bottom lines being reported: The net effect of the May adjustments reduced net earnings by $21,000 out of a pooled total of $773,152 or 2.7% (T.1260). In accounting terms, Natelli felt the adjustment was not material (T.1907). After reaching a tentative conclusion, he discussed the problem with his partner, Leon Otkiss, who had been assigned to review the proxy statement to be certain it conformed to SEC requirements (T.1741-42). Under the policy of PMM, a partner such as Otkiss was assigned to review public filings because he had special expertise in the application of accounting rules and regulations (T.1741-42). After discussion, Otkiss agreed with the conclusion reached by Natelli (T.1907).

Natelli then redrafted the footnotes, eliminating what he and Otkiss had concluded were two unnecessary extra lines —those specifically describing the retroactive adjustment (T.1905-08)—and made those adjustments in the revised note, in the same line with the adjustments caused by the retroactive poolings. This revision did not change the bottom lines at all, which continued to reflect accurately the total net sales and net earnings after all adjustments (T.1212).

Before he finalized his revision of the footnote, but after he had decided to make the change, Natelli discussed his decision with Scansaroli. Scansaroli concurred—that is, he accepted Natelli's conclusion that combining the reduction of earnings because of the Michaels contracts with the increase due to the tax credit created an "immaterial" difference which did not require elaboration in the trend of earnings footnote drafted by Natelli; but as he knew, the matter would have to be—and in fact was—discussed with the PMM SEC reviewing partner, Leon Otkiss (T.884, 1909).

b. The Unaudited Statement of Earnings.

During the course of his work in May on the aborted proxy statement, Scansaroli reviewed, but, neither he, nor anyone from PMM was called upon to audit NSMC's contracts-in-progress. He believed some of the contracts to be questionable (T.1670-72), memorializing his views in the workpapers (GX 13, E.105), but because the proxy statement was abandoned, further inquiry was not pursued at that time (T.1674-75).

When the proxy statement was revived in August, a current review was needed, and Scansaroli assigned Oberlander to the task (T.749). After completing his review, which was *not* an audit, Oberlander concluded that some of the contracts should not be included in the company's nine-month figures, including some of the same contracts questioned by Scansaroli three months earlier (GX 13, E.116-17).* Oberlander sought to discuss his conclusions with Kurek, then NSMC's vice president and treasurer, but Kurek, declined to discuss the contracts with Oberlander: "Let's just stop right here, get somebody that's got some authority to come over and go through it with me." (T.266-67). Oberlander turned over his workpapers to Scansaroli, who met with Kurek and reviewed the contracts Oberlander had questioned (T.407-09).

On the basis of his discussion with Kurek, Scansaroli insisted that approximately thirty (30%) percent of the questioned amount (represented by three Syntex contracts) should be—and subsequently was—written off. Also based on his conversation with Kurek, Scansaroli saw no reason why the other questioned contracts could not properly be included in NSMC's unaudited financial statements (T.1551-53). Kurek testified that his conversation with

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* Oberlander also concluded that some of the contracts were *understated* as reflected in the company's statement (T.800).

Scansaroli represented a good faith effort by the two of them to portray accurately NSMC's financial condition (T.408-09).

Summary of Argument

> I must say that treating as the law and common sense requires us to do, each defendant's case taken separately, I believe Scansaroli has somewhat of a good argument here. . . . It is a close question, I think frankly as to Scansaroli, as I see it. Certainly if I were the factfinder, I would be more troubled with his case for a variety of reasons. . . .

Judge Tyler, after both sides had rested (T.2134-35).

The trial court's view of the case with respect to Joseph Scansaroli represents the starting point for our analysis. We respectfully submit that the sum total of the facts adduced at trial establish not only that this was "a close question" as to Scansaroli, but indeed, that no reasonable jury could fairly conclude, beyond a reasonable doubt, that Joseph Scansaroli: (a) participated in a criminal act with respect to the footnote; or (b) made an accounting judgment permitting NSMC to include in sales certain contracts-in-progress with the requisite criminal intent. The case should not have been submitted to the jury, and in any event the evidence was insufficient to support the conviction.

Moreover, the error in submitting the case to the jury was compounded by other errors committed during the trial: The trial court improperly admitted against Scansaroli testimony that was rank hearsay as to him (Point II, *infra*); after ruling that the government would *not* be permitted to offer so-called "fraud victim" testimony, the trial court permitted the government to do just that (Point III, *infra*); and the trial court instructed the jury that it might convict the defendants if it found they had

aided and abetted NSMC officials in filing a false proxy statement, but *refused* to define "aiding and abetting" for the jury (Point IV, *infra*).

We submit that a "question" which did not even rise to the level of being "close"—the innocence or guilt of Joseph Scansaroli—was decided in the context of substantial trial errors. The result has been the destruction of an unblemished professional career. The conviction of Joseph Scansaroli should be reversed.

POINT I

The evidence adduced at trial was legally insufficient to support the conviction of Scansaroli.

> . . . I think you [Scansaroli and Natelli] are absolutely sincere when you say that you do not believe that you did anything wrong in this *audit or audits* for National Student Marketing. After thinking about the matter for a long time I think you honestly mean that. But the tragedy is that the jury found that this was an *audit or audits* done with reckless disregard for what was really involved. We know that because of the record showing what it did in the jury deliberation. (Emphasis added)

Judge Tyler, on sentencing Scansaroli and Natelli, December 27, 1974 (A.284).

As Judge Tyler's remarks make plain, the jury found that an *audit* was improperly—"recklessly"—done. But the only audit which was before the jury occurred in October, 1968, well before the alleged criminal acts took place. No charge was made that that audit of the 1968 financial statements of NSMC constituted criminal conduct on the part of Scansaroli or Natelli. Thus, the real tragedy here is that Scansaroli was convicted for conduct not charged as a crime: his performance on the 1968 audit.

The indictment charged that NSMC's 1969 proxy statement was false in two respects: (1) that the statement of earnings for the year ended August 31, 1968 (which had been audited in 1968), as it appeared in the 1969 proxy statement, was materially false and misleading because it failed to contain in a footnote, narrative disclosure that certain contracts originally reported as income for that period had subsequently been written off by the company; and (2) that the *unaudited* statement of earnings for the period ended May 31, 1969 overstated sales and earnings. This latter allegation was based on: (1) the inclusion in net sales of a $519,000 Eastern Airlines contract; and (2) the inclusion in the unaudited financial statements of certain contracts questioned by Douglas Oberlander during a review in August, 1969 of the financial statements for the proxy statement.

A review of the evidence as it relates to these specific charges of the indictment shows: (1) that the decisions concerning the footnote were made by Scansaroli's superiors Natelli and Otkiss, and that Scansaroli had no meaningful role in its preparation; (2) Scansaroli had absolutely nothing to do with the decision to record the Eastern contract as income; and (3) the decision with regard to the commitments challenged by Oberlander were made by Bernard Kurek, the chief government witness, and Scansaroli in complete good faith. There was no contrary evidence.

Thus, the specific charges against which Scansaroli defended had nothing to do with the conduct of any audit. Why, then, was Judge Tyler led to the conclusion that Scansaroli was convicted because "this was an audit or audits done with reckless disregard?" (A.284). To what audit was Judge Tyler referring? The answer is not difficult to find. The evidence adduced at trial was so palpably lacking, so woefully insufficient to show that Joseph Scansaroli participated in any criminal conduct in connection with the *1969* proxy statement, that the government fell

back on filling the record with evidence concerning PMM's *1968* audit of NSMC, the only NSMC audit Joseph Scansaroli worked on, but one which has *never* been charged to have involved the commission of a crime.

It may be that the trial evidence showed Scansaroli to have acted foolishly, perhaps even negligently, in his work on the 1968 audit; indeed, he candidly testified at trial that he had been "too easily satisfied" in *1968* (T.1660-61). But even if he was, that conduct was never charged to be criminal.

Rather, the actual charge against Scansaroli was that he participated in the preparation of the footnote to NSMC's restated 1968 earnings (GX 25, E.167) in order to conceal the Michaels write-offs, and that he permitted NSMC to include in its unaudited nine-months' financial statements a commitment from Eastern Airlines, and a large portion of the contracts-in-progress Oberlander had questioned. The government's theory was that Scansaroli committed this 1969 crime in order to cover up the fact that he had been "too easily satisfied" during the 1968 audit.

Examination of each of these four elements, however—the footnote, the Eastern commitment, the questioned contracts and the motive—will show that the government's bucket does not hold water.

The Footnote

The government contended that the defendants prepared the footnote for the proxy statement in order to hide the fact of the Michaels write-offs. By lumping the defendants together—as was its wont throughout—the government's contention that Scansaroli participated in the preparation of the footnote attained a sheen of plausibility. Once the evidence is prized apart, however, its legal insufficiency as the basis for inferences with respect to Joseph Scansaroli becomes readily apparent.

Viewed in the light most favorable to the government, the only evidence illuminating Scansaroli's role in the preparation of the footnote is the following:

—Scansaroli's preparation of the underlying work papers containing the raw data later inserted in the footnote (GX 13, E.97);

—Scansaroli's general responsibility as PMM supervisor on the engagement (T.1481-82);

—Natelli's testimony that he*, *not* Scansaroli, drafted the footnote (T.1905-08);

—Natelli's testimony that he and Otkiss *not* Scansaroli, made the decision not to show the write-offs on a separate line (T.1905-08);

—Natelli's testimony that Scansaroli "possibly may" have been the one who inserted the figures into the footnote drafted by Natelli (T.2068).

It is clear from this recital that there was insufficient evidence to permit the jury to infer that Scansaroli was in any way responsible for either preparation of the footnote or the decision to include the adjustment for Michaels write-offs in the line with the adjustments resulting from the poolings. So far as preparation of the footnote is concerned, the uncontradicted evidence established that it was drafted by Natelli; Natelli's testimony that Scansaroli "possibly may" have filled in the figures is not sufficient to permit the inference that Scansaroli did. Nor does Scansaroli's testimony that it was his job "with the people that were working with me to *accumulate* . . . figures" for the proxy statement as a whole (T.885) permit the inference that it was Scansaroli who

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* We do not imply that Anthony Natelli was motivated in drafting the footnote, or in making the relevant decisions, by anything more than his sense of professional responsibility.

inserted or even caused the *insertion* of the specific figures in the footnote. That Scansaroli gathered numbers, in raw form, as reflected in his work papers, does not show what was done with those numbers, nor by whom; and generalized supervisory "responsibility" can hardly substitute for evidence—direct or circumstantial—of the performance of a specific act.

Once again, however, the government sought to disguise the insufficiency of its case against Scansaroli by fusing the defendants. Thus, the government contended that it was no defense that the defendants cleared this matter with Otkiss. The "defendants" were deprived of this defense, the government argued, not because of anything Scansaroli did or omitted, but because of a conversation which Natelli had with Otkiss.

At its very worst, the evidence showed that Scansaroli participated in the early stages of a complex decision-making process. It did not show that Scansaroli drafted the footnote, revised it or inserted any numbers. This showing could not enable a reasonable jury to fairly conclude that Scansaroli's participation in the preparation of the footnote was sufficient to attach criminal liability.

In its effort to somehow tie Scansaroli to the preparation of the footnote, the government reached back to his preparation of a proposed journal entry in May, 1969. The government—although never explaining how the journal entry, which was an internal matter for NSMC, affected the preparation of the footnote—argued that the journal entry gave birth to the "phony" tax credit *and* "was designed to avoid disclosure of the loss" resulting from the discovery by NSMC officials of Ron Michaels' dishonesty. What evidence did it offer?

First, the entry itself. On its face, the entry flatly contradicts the government's argument and provided nothing from which the jury could infer concealment. On the contrary, the journal entry recites:

> Based on subsequent facts, it was decided to adjust 3 Contracts entered into by Ron Michaels: (1) Clairol, (2) Cheseboro and (3) Ban. (GX 13, E.98)

Second, the elimination of the deferred tax provision. The government's argument was that Scansaroli concocted a "phony" tax credit that could then be used to offset the Michaels losses, reducing the net effect to more readily concealable proportions. The government's "motive" in flailing against the tax credit was transparent: If the tax credit was real—as Scansaroli and Natelli believed—then the net effect of the adjustment *down* as a result of the Michaels contracts and *up* because of the tax credit was indeed immaterial—earnings of $21,000 out of a total of $773,152.

But there was nothing in the record from which a reasonable jury could infer that the tax credit was "phony" or that Scansaroli knew it was "phony." As described in detail above (pp. 10-12), the tax credit was conceived and suggested not by Scansaroli, but by a PMM tax expert—Carol Raimondo (T.1386)—whose contemporaneous memorandum memorialized her conception (NX O, E.482). And she, and Scansaroli and Natelli, discussed the credit with and received the concurrence of a PMM tax partner, Eugene Holloway (T.1386, 1541, 1859). That Mrs. Raimondo later appeared to have been in error does not even begin to prove that Scansaroli knew she was wrong in May, 1969, let alone that *he* fabricated the tax credit as a concealment device. In short, and in fact, the tax credit was not a "phony"* and Scansaroli could not, therefore, have known it was "phony."

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* The government's argument that the tax credit was "phony" rested entirely on testimony by Scansaroli that he later concluded that Mrs. Raimondo and Mr. Holloway were wrong (T.1690). The brief on behalf of Natelli (Point III) demonstrates the seriousness of the error in allowing the government to argue that the tax credit was "phony" (T.2287, 2316) when *no* evidence was introduced to support such a prejudicial and inflammatory contention.

Finally, says the government, if the journal entry was innocently prepared, Scansaroli would not have reduced the tax adjustment from $190,000 to $188,750 so that the amount of liability being eliminated precisely equalled the loss on the Michaels contracts. The jury could infer, the government argued, that Scansaroli changed the numbers to conceal the loss (T.2288).

Within a week of the first journal entry, Scansaroli prepared a second journal entry to write off the fourth non-existent Michaels contract (T.1542-43). This second entry contained no offsetting credit of any kind: It simply created a loss which was being treated retroactively because the company reported to the auditors that the underlying "contract" did not exist. More importantly, Scansaroli was charged with concealing the loss created by these two journal entries in the *footnote,* as part of the proxy statement, and *not* in the entries themselves, which were not designed to be seen and were never seen by the public. The charge in this indictment would not change by such much as a single word if the tax credit had been entered in the amount of $190,000, rather than $1,250 less, whatever the reason for the reduction. Nor does the subtraction of $1,250 at the time Scansaroli prepared the proposed adjusting entry, permit any inference with respect to Scansaroli's state of mind in connection with the preparation, three months later—by someone other than Scansaroli—of the footnote itself or of the unaudited 1969 earnings statement.

In any event, after preparing the requested journal entry, Scansaroli presented it to and discussed it in detail with NSMC's controller, government's witness John Buck. Scansaroli reviewed the underlying facts with Buck, who was at least as familiar with them as Scansaroli was, and informed Buck of the tax credit suggested by PMM's tax experts (T.642-46). Buck was free to accept or reject the "suggested" adjustments; with full command of the facts, it was Buck—and *not* Scansaroli—who ultimately decided

how the entry should be reflected in the company's books (T.636, 642, 660-61, 663-64).

The Eastern Commitment

The evidence at trial showed plainly that Scansaroli had nothing to do with the decision to include the Eastern commitment in NSMC's nine-months' financial statement:

—The Eastern commitment was discussed among Natelli, Kurek and Randell at the printer's plant while Scansaroli, together with several others, was working on wholly unrelated matters (T.1559-60, 1919-21).

—Scansaroli left the printer's *before* the written commitment from Eastern arrived and *before* any decision to include it was made by anyone (T.1561, 1927-28).

As Judge Tyler put it:

> The government somehow argues something about Scansaroli being involved in the evening in [the printer's]. At least I read it that way . . . I don't understand that Scansaroli was there at all doing these things about the Eastern deal and all that. He was there, but he wasn't doing this kind of thing. . . . And no one said to the contrary. (A.255).

In short, there was no evidence to connect Scansaroli in any way to the inclusion of the Eastern commitment. But the prosecutor was not content to allow the jury to consider Scansaroli without attempting to connect him—no matter how—to the Eastern contract. Thus, the prosecutor's argument in summation, that Scansaroli *was involved* "in the middle of the night" at the printer's plant, shabbily distorted the record, thereby violating his duty as a public prosecutor. *See, Berger* v. *United States,* 295 U.S. 78 (1934); *United States* v. *Bugros,* 304 F. 2d 177 (2d Cir. 1962). Moreover, the use of a metaphorical refer-

ence to a "doctor at three o'clock in the morning down in his cellar burying a fresh corpse" (T.2285-86; see also, T.2268, 2295, 2296, 2304) is precisely the sort of innuendo that leads a jury to view events only in other than the context in which they occurred. To be hard at work on a proxy statement at a printer's plant in the early morning hours needs—or should need—no defense because of the commonplace nature of this activity.*

The Contracts Reviewed by Oberlander

The major portion of NSMC's unbilled accounts receivable at May 31, 1969 challenged by the government was represented by the Eastern commitment. As shown above, Scansaroli played no role in the decision to include that commitment in NSMC's revenues and earnings.

The remaining portion of the challenged unbilled receivables at May 31, 1969 can be found in the Oberlander work papers (GX 13, E.116-17). These work papers reflect Oberlander's judgment that certain of the unbilled receivables were either "bad" ($179,669 in gross profit) or "questionable" ($25,000 in gross profit) at May 31, 1969. During a similar review of contracts-in-progress in May 1969, Scansaroli believed that some of these same contracts were questionable (T.1669-72).

Following Oberlander's review, Scansaroli met with Kurek to discuss the status of the contracts listed on Oberlander's schedule. On the basis of his discussion with Kurek, Scansaroli insisted that approximately thirty (30%) percent of the questioned amount (represented by three Syntex contracts) should be—and subsequently was—written off. Also based on his conversation with Kurek, Scan-

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* The prosecutor also sought to create the impression that there was something sinister in the fact that certain entries were made after the close of the fiscal period—an occurrence which all of its witnesses acknowledged to be proper. (Compare T.2208, 2269 with T.663-64, 782).

saroli raised no objection to the inclusion of the other questioned contracts in NSMC's unaudited financial statements (T.1551-53). In short, as Kurek testified, he and Scansaroli reviewed the matter in an effort, as accountants, to come to a decision which reflected the financial picture of the company (T.408-09).

Scansaroli acknowledges both the occurrence of these events and his participation in the ultimate judgment not to object to the inclusion by NSMC in its unaudited financial statements of the balance of the contracts questioned by Oberlander. But participation in this decision to permit the company to continue certain commitments in its unaudited figures* was insufficient for conviction unless it was made with criminal intent, and with knowledge that the items were material.**

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* The brief on behalf of Natelli (Point II B) points up the error of the trial court in failing to instruct the jury properly on the distinction between the accountants' responsibility for unaudited figures—such as these—and audited statements. This directly relates to Scansaroli as the only evidence of participation by him in anything claimed to be criminal related to unaudited statements.

** The Natelli brief also demonstrates how the trial court erred in failing to instruct the jury that they had to find that Scansaroli *knew* the statement in question was *material*. The court was specifically requested to instruct the jury that they had to find such knowledge before they could convict (Scansaroli Request No. 12, A.226-27). In this regard, the government never contended that the contracts questioned by Oberlander were themselves a material element of the unaudited financial statement. Rather, the government's attack on the unaudited statement was primarily based on its contention that it was improper to include the Eastern commitment—a matter which did not involve Scansaroli. Did the jury's finding as to Scansaroli rest solely on the Oblerander-questioned contracts, or on Natelli's decision to permit the Eastern commitment, or both? We have no way of knowing. Therefore, it is impossible to conclude, even if the charge be deemed sufficient, that Scansaroli *knew* that a false statement was made and that the statement was *material*.

Motive and Intent

The government contended that Scansaroli's criminal intent—his knowing and willful participation in the preparation of this portion of the nine-months' unaudited financial statement—was established by his statements to Kurek and Natelli which the government suggested reflect Scansaroli's concern that he was in danger of losing his accounting certificate as a result of his work in confirming the contracts-in-progress during the 1968 audit. But this supposed motive would have had nothing to do with the unaudited nine-months' figures, although it may have had a connection with the footnote—if Scansaroli had anything to do with its preparation. In other words, it is inconceivable that Scansaroli, concerned about his license, would look the other way while the company issued statements containing contracts he believed were bad.

What proof did the government offer to show Scansaroli's intent and motive? The government offered evidence of remarks made by Scansaroli to Kurek during lunch one afternoon in June or July, 1969 that perhaps he should put his certificate in "*a locked box*" because ". . . he didn't know whether the right decision or the right type of accounting had been made back in August [1968] . . ." (T.237) and that at one point he jokingly said to Natelli: "Hope we don't lose our certificates over this one." (T.1933).

This was not an adequate basis to permit the jury to conclude that Scansaroli possessed the requisite criminal intent. For despite what these statements *might* have meant, the uncontroverted facts—which are not so open to competing interpretations as are the two possibly joking, possibly serious, statements of Scansaroli—establish that Scansaroli was not possessed of criminal intent. Whatever Scansaroli's *words* meant, his *conduct* was consistent and honest.

Thus, the government's witness Oberlander testified that Scansaroli, who had broad responsibilities in connection with the proxy statement and could have assigned Oberlander to virtually any portion of the work to be done and could have reviewed the contracts-in-progress himself, specifically assigned him to review the very matter the government says concerned Scansaroli the most: contracts-in-progress (T.749).

And Johnston, another government witness, testified that after he was assigned to the *1969* audit of NSMC, Scansaroli (who had left PMM in October to go to work for NSMC), rather than expressing apprehension as might be expected of one concerned about losing his license, in fact suggested *additional* audit steps—specifically, in connection with Johnston's examination of contracts-in-progress (T.977-80).

Similarly, Scansaroli's conduct with respect to his work papers for the 1968 audit (GX 3, 4A, 4B, 4C) reflecting matters he supposedly was anxious to hide—to the point of committing a crime, according to the government's theory—contradicts any notion that Scansaroli possessed criminal intent. For rather than using a shredder, he had used a stapler; rather than destroying or doctoring that which the government argued would damn him, he had meticulously preserved it. And when access to these work papers was requested by someone unconnected with Peat, Marwick, Scansaroli unhesitatingly showed those workpapers reflecting his review of the contracts-in-progress to Arnold Berman, a CPA acting on behalf of a company which NSMC proposed to acquire (T.1413-15).

This undisputed evidence of his conduct with Oberlander, Johnston, Berman and the work papers plainly foreclosed even the possibility that Scansaroli seriously felt that his license was in jeopardy, and represents conduct on Scansaroli's part which is the antithesis of any effort to cover up past mistakes.

This pattern of conduct—by a man whom the government argues was fearful to the point of participating in a cover-up—culminated in Scansaroli's appearance before the SEC during its investigation. When called, Scansaroli, without seeking the protection of counsel, as might be expected of a man who thought he had done something wrong, testified on three separate occasions, answering each question to the best of his ability.

The government will no doubt contend that its burden to prove Scansaroli's criminal intent was satisfied by proof of his "recklessness." This simply will not do. As set forth in the brief on behalf of Natelli (Point II A), proof of recklessness is not sufficient to establish that a defendant acted "wilfully and knowingly." In any event, the only conduct by Scansaroli which the government argued was reckless was Scansaroli's work in connection with the *1968* audit, not the *1969* proxy statement. But it was only the latter, and not the former, which was charged as criminal. Consequently, proof of recklessness, which is limited by the government's own evidence to the *1968* audit, has no bearing on Scansaroli's intent on the charges here.

The plain fact is that Joseph Scansaroli was convicted of participating in an *audit* the jury believed to have been conducted recklessly. What all this adds up to is more than a simple matter of conflicting evidence from which the jury might or might not have inferred Scansaroli's criminal intent in 1969. For the issue was whether there was sufficient evidence from which the jury could fairly—and beyond a reasonable doubt—conclude that Joseph Scansaroli made one accounting judgment in 1969 with the requisite criminal intent. We respectfully submit that the government's own evidence demonstrates compellingly that the answer must be "No."

POINT II

The court erred in admitting testimony that was pure hearsay as to Scansaroli.

During the course of the trial a series of meetings was unfolded before the jury between Kurek and Randell (T.150-51, 220, 223), Kurek and Natelli (T.231-34) and Kurek, Randell, Natelli and others (T.238). At first, this evidence was received subject to connection; subsequently, without proper connection and over vigorous defense objection, it was ruled admissible against Scansaroli (T.1162-63), to prove his knowledge of the situation with respect to NSMC's contracts-in-progress. The testimony and exhibits admitted subject to connection—and later received in evidence against Scansaroli—were the following:

1. A meeting between *Kurek* and *Randell* on March 1, 1969, at which Kurek told Randell that various account executives had reported that approximately $1 million of commitments booked as of August 31, 1968 and November 30, 1968 "were not any good" (T.220). The proposed agenda for that meeting (GX 9, E.66) was also admitted.

2. A meeting between *Kurek* and *Randell* on March 8, 1969, at which Kurek told Randell that NSMC could show a loss of up to $1,700,000 "if the commitments which had been reported as bad were removed from the books" (T.223).

3. A schedule of projected profit and/or loss (GX 10A, E.92) which *Kurek* and *Randell* discussed on March 8, 1969, a copy of which was sent to Natelli (T.222).

4. A meeting in mid-March between *Kurek, Randell* and *Natelli* during which Kurek's projections were discussed, and at which Randell stated that NSMC

would not show the loss Kurek projected and that he knew of other commitments and contracts "that the salesmen were working on" (T.225).

5. A conversation between *Kurek* and *Natelli* on June 3, 1969, during which Natelli stated that the unbilled receivables at year end 1969 could be as high as $4 million and that unbilled receivables could make or break the company (T.233-34).

6. A June 9, 1969, NSMC Finance Committee meeting attended by *Randell, Kurek* and *Natelli,* during which Natelli voiced concern over the collectibility of the remaining commitments. (T.242-48). Partial notes of this meeting, transcribed by an unnamed NSMC secretary, were also admitted (GX 16, E.130).

Scansaroli did not attend any of these meetings, was never informed of the substance of the conversations and discussions that occurred at the meetings, and never saw any of the documents relating to the meetings that were admited as government exhibits. In addition, there was no evidence—direct or circumstantial—of any criminal ties between Scansaroli and Kurek or Randell. In short, the jury was permitted by the admission of this rank hearsay to impute to Scansaroli that knowledge possessed by Randell, Kurek and Natelli derived from those meetings simply because he was an employee of independent auditors who were routinely "involved" with management—an involvement which the trial court conceded "wasn't criminal" (T.1162-63).

Judge Tyler admitted the evidence on the novel theory, founded on no authority, that an employee of an independent accounting firm constructively possesses the knowledge held by members of the management of the firm's client companies, and by the partners of the accounting firm, regardless of the total absence of any direct or indirect

connection:

> The Court: I am going to receive it beyond that status because I believe that the record is now clear enough that everybody necessarily in PMM was obviously working with management and they are all in this together.
>
> That doesn't mean they are all in this together criminally, of course. But I think it is sufficient unto the day to admit this as to Mr. Scansaroli even though he may have had no direct responsibility in part or he may have. Even if he did, it wasn't criminal. I understand that.
>
> When accountants work with management on an audit, they are all busily involved together. For that simple reason alone the subject to connection ruling in the early stages I don't think is b[illegible]ding now. . . . (T.1162-63).

When counsel called the court's attention to the fact that the communications at issue took place months after the 1968 audit had been completed and months before the 1969 audit had begun, the court replied: "That may well be. But again, Peat, Marwick was still the outside accountants of this firm, NSMC. Not only that, there was work going on in the usual course"* (T.1163).

The court's ruling that, as a matter of law, Scansaroli was "connected" *solely* by reason of his *employmen* with PMM, regardless of its association with management, constituted reversible error.

Under clear and unambiguous principles repeatedly articulated by this Court, the reception of this hearsay evidence was improper:

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* The court's error was compounded by this modification, since the "work going on in the usual course", at least until the end of April, 1969, was not being performed by Joseph Scansaroli (T.1522-23).

> The threshold requirement for admissibility is satisfied by a showing of a likelihood of an illicit association between the declarant and the defendant. . . .

United States v. *Ragland,* 375 F.2d 471, 477 (2d Cir. 1967). *See also United States* v. *Geaney,* 417 F.2d 1116, 1119 (2d Cir.), *cert. denied sub nom. Lynch* v. *United States,* 397 U.S. 1028 (1969).

Here there was no evidence to even bring Scansaroli close to the "threshold"; not only was there no showing of an "illicit association" between Scansaroli and any of the declarants, but there was an explicit recognition by the trial court that no such "illicit association" had been shown:

> That doesn't mean they are all in this together criminally, of course. But I think it is sufficient unto the day to admit this as to Mr. Scansaroli even though he may have had no direct responsibility in part or he may have. *Even if he did, it wasn't criminal.* I understand that. (T.1162-63) (Emphasis added)

There was thus no basis in law or in fact for receiving the declarations of Kurek, Randell and Natelli against Scansaroli.* This constituted clear error.

POINT III

Despite its own ruling to the contrary, the trial court erroneously permitted "fraud victim" testimony.

> I must say that treating as the law and common sense requires us to do, each defendant's case taken

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* Scansaroli's pre-trial motion for a severance of his case from Natelli's was denied (T.5-13). Although the motion to sever was predicated on anticipated testimony regarding remarks made by Scansaroli being offered with respect to his alleged motive, nevertheless, a severance might have avoided the problems created by the admission of the hearsay testimony described above.

> separately, I believe Scansaroli has somewhat of a good argument here. . . . It is a close question, I think frankly as to Scansaroli, as I see it. Certainly if I were the factfinder, I would be more troubled with his case for a variety of reasons. . . .

Judge Tyler, after both sides had rested (T.2134-35).

In a close case, such as this one, even the slightest error can tip the balance. The trial court's egregious error in permitting irrelevant "fraud victim" testimony may well have toppled the scales.

In its opening statement, the government explained to the jury that it would prove that people relying on the proxy statement had permitted their "little businesses" to be "gobbled up" for NSMC stock (T.31, 47). Thus, the government intended to elicit, as part of its case-in-chief, testimony from shareholders of acquired companies "that they would not have permitted [their] . . . deal[s] to go through had they known the true state of affairs" (T.697).

In response to defendants' motion to exclude "fraud victim" testimony, the court correctly ruled that the government had no burden to prove reliance and that, accordingly, "fraud victim" testimony was irrelevant and immaterial to any essential element (T.701-02). No such testimony should have been permitted.

The court enunciated its decision during the following colloquy:

> Mr. Velie: I believe that you have accurately stated the Government does not have to prove reliance.
>
> The Court: There is a problem for the defendants. It is very easy for the Government in this context to get somebody to come in, particularly when the stock went down, and some of these sellers who sold these companies to NSMC are hopping mad. Their stock turned out to be worthless, or relatively so, and they

didn't do so well. Therefore it puts the defendants at a terrible disadvantage.

There is a second problem. You have got to prove that the defendants perpetrated a fraud. You promised this jury that that is what you would do. I don't blame you. But I don't think that is helped by having somebody come in here and testify to an ultimate question which the jury itself will decide.

In other words, the witness will in effect be deciding for the jury, in a sense, one of the most important questions in the case, and I don't think that is normally done in our court.

We don't let somebody come in and say, 'Look, jury, if I had to decide your question, I would decide it such and such a way.' (T.701).

Thus, defendants' motion to bar the use of "fraud victim" testimony was decided in their favor:

The Court: I think the defendants have the better of the argument and I won't permit such testimony from any witness, whether he is an ordinary stockholder or a stockholder by virtue of the sale of his company to NSMC.

Mr. Velie: Your Honor, in that case I will not offer any 'What would you have done' testimony.

The Court: All right. (T.702).

Unfortunately, the trial court soon fatally diluted its own ruling by permitting the very sort of testimony it had ruled immaterial. The most blatant example was the testimony of the government's witness Louis Schauer, an attorney for Interstate National Corporation, who was permitted to testify, over defense objection, as follows:

Q. Did you know that of the $1.7 million of unbilled accounts receivable booked by National Student Marketing in 1968, over $1 million had been written off as uncollectible and no good?

Mr. Stillman: I object, your Honor.

The Court: Overruled.

A. No.
Q. You didn't know that?
A. No.
Q. Did you know that of $3.3 million of unbilled accounts receivables booked in the 18-month period including the year 1968 and the half year of 1969, $3.3 million of unbilled accounts receivable had been booked and $2 million or more had been written off as uncollectible or no good?

Mr. Stillman: I object to this. I submit it accomplishes the very thing that we have been trying to prevent.

The Court: No, Mr. Stillman. I'm sorry. I disagree.

The objection is overruled. You certainly are free to argue that these facts aren't true in any event. That doesn't mean he can't ask the question.

Mr. Stillman: It is something I would like to take up with your Honor—

The Court: No, we have taken it up quite a bit. We don't need to take it up any more.

Mr. Stillman: Surely.

A. No.
Q. You didn't know that?
A. No. (T.1058-59)

* * *

Q. The effect of that deal was, was it not, that the 1300 or so shareholders of Interstate gave up their investment in the insurance company and received instead shares of National Student Marketing stock?

Mr. Stillman: Same objection, your Honor.

> The Court: Just a moment. I will allow it. As a result of the closing, I would prefer you rephrase it.
>
> Q. As a result of the closing, Mr. Schauer, 1300 shareholders of Interstate gave up their investment in the insurance company and received instead shares of stock of National Student Marketing, is that correct?
>
> A. They exchanged their shares of Interstate for shares of National Student Marketing, that's right. (T.1060-61)*

Thus, the trial court not only permitted the introduction of immaterial evidence but allowed the Government to evoke, in the jury's mind, sympathy for the "little businesses" which had been "gobbled up" by NSMC.

This Court has made a clear distinction between those cases, such as the one at bar, where the profit or loss suffered by a third person is irrelevant to the crime charged, and those "mail fraud" cases where "proof of the worthlessness of the stocks sold to the public may have some tendency to prove the fraud charged." *United States* v. *Minuse,* 142 F.2d 388, 390 (2d Cir.), *cert. denied,* 323 U.S. 716 (1944).

In *Minuse,* a case involving illegal stock manipulation (Section 9(a) of the Securities and Exchange Act of 1934, 15 U.S.C. § 78i(a)), the government had been permitted to offer testimony of a few witnesses concerning losses they sustained as a result of the defendants' manipulations. In an opinion written by Judge Hand, this Court stated:

> Admission of the testimony was plainly erroneous. Whether the appellants' manipulative practices caused profit or loss to anyone trading in [the] stock was irrelevant to the crime with which they were charged.

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* Testimony of a similarly prejudicial nature was given by the government's witness Arthur Frommer (T.1014-31), who sold his business to NSMC.

> Therefore it was wholly unwarranted to bring in testimony of losses; such testimony could only confuse the issues and might unfairly influence the jury. In a case of this character there is much less excuse for parading "victims" than in mail fraud cases, where proof of the worthlessness of the stocks sold to the public may have some tendency to prove the fraud charged against the defendants. Even in mail frauds we have said that the use of 'victim' testimony may easily be abused and must not be carried to extremes in order to work upon the sympathy of the jury. United States v. Brown, 2 Cir., 79 F.2d 321, 324, certiorari denied 296 U.S. 650, 56 S.Ct. 309, 80 L.Ed. 462. (142 F.2d at 390)

The convictions were not reversed because, unlike the present case, the losses mentioned were minimal ($160 and $500) and the evidence of the defendants' guilt—far from presenting the "close question" Judge Tyler observed this case does—was overwhelming.

In *United States* v. *Brown*, 79 F.2d 321, 324 (2d Cir.), *cert. denied sub nom. McCarthy* v. *United States*, 296 U.S. 650 (1935), prejudicial "victim" testimony was injected into the trial, and this Court severely admonished against its use:

> [T]he prosecution succeeded in getting before the jury that in consequence of their losses some buyers had lost their homes and their business, and gone hopelessly into debt; that they had lost everything including their friends, and were destitute; that their losses went into millions; that one unfortunate had committed suicide. Were the guilt of the accused not so irrefragably shown, we could not affirm the judgment in the face of this, and we wish to make it clear that we have never given warrant to any such abuse.

See also United States v. *Grayson*, 166 F.2d 863 (2d Cir. 1948).

In sum, the "victim" testimony introduced at trial, in spite of Judge Tyler's early—and correct—decision to exclude it, was plainly irrelevant and could serve only to inflame and prejudice the jury against the defendants. Moreover, the harm done was severely aggravated when the prosecutor, in his summation, made pointed reference to precisely the testimony he should not have elicited in the first place:

> Ask yourselves, would you go and sell your house, your family's business, take the money out of the savings bank, borrow against life insurance, and buy that stock? Ask yourselves if you would do anything like that.
>
> Well, the defendants knew all of those things and they didn't warn anybody, and they knew people were relying on this. Mr. Frommer in fact did go out and sell his business for National Student Marketing stock because they never warned him. . . . You may find that he got cheated. (T.2306).

Such unabashed efforts on the part of the government to arouse the jury's passions, to inflame its instincts, to prevent it from focusing its attention on the elements of the charge, particularly in a case conceded by the trial court to be a close one, must not be countenanced. *See United States* v. *White,* 486 F.2d 204, 206 (2d Cir. 1973), *cert. denied,* 415 U.S. 980 (1974); *United States* v. *Grunberger,* 431 F.2d 1062, 1067 (2d Cir. 1970).

POINT IV

The court erred in instructing the jury that it could convict the defendants as aiders and abettors and then refusing to define aiding and abetting.

At the close of the government's case, the trial court explicitly recognized that the government's theory with respect to Natelli and Scansaroli was that they had aided and

abetted the management of NSMC in filing a false proxy statement:

> [W]hat was going on here is that management decided to insist on presenting a fraudulent picture through its proxy statement in order to support its program of aggressive acquisition of other companies, mergers and the like, and that finally the management tips overboard the good sense and judgment of the defendants or one of them here and the defendants according to the Government's theory, further *aided and abetted* in this scheme which was primarily in the first instance at least management dominated.
>
> Is that a fair statement of the Government's case?
>
> [The Prosecutor]: Yes, your Honor.
>
> (T.1340) (Emphasis added)
>
> * * *
>
> [Y]our contention is that the two defendants here on trial were *aiding and abetting* Cort Randell, Kurek and others?
>
> [The Prosecutor]: Absolutely.
>
> (T.1342) (Emphasis added)

And the trial court squarely placed this issue—aiding and abetting—before the jury, in two separate portions of its charge: First, in defining the elements of the charge against Scansaroli and Natelli:

> [I]f you did find that [the defendants] either knowingly made these mis-statements or they caused them to be made or they *aided and abetted* in their making, then you would be obliged to convict the defendant or defendants for which you make these findings. (T.2341) (Emphasis added)

And second, in describing the government's contentions:

> [T]he government argues . . . that [the defendants] were very anxious to assist management, even to the

> point of *aiding and abetting* management in filing false earnings figures with the Securities and Exchange Commission. (T.2372-73) (Emphasis added)

Notwithstanding these instructions, and even though he had been explicitly requested to do so, by the defense *and* the Government both *before* (T.2148, Gov't Request No. 10, A.152-53) and *after* charging the jury, the trial court refused to define "aiding and abetting" or to guide the jurors in their deliberations:

> Mr. Stillman: Your Honor, I don't believe that at any point in the charge you advised the jury with respect to the aiding and abetting statute—
>
> The Court: I didn't. I purposefully left that out. . . . What I did do, however, and I did it having in mind one of your requests, I gave them in substance, although I would be the first to say not as eloquently as the Court did in such a celebrated case as U.S. vs. Peoni, a case known by heart to all former assistant United States attorneys, like you and me—I didn't go into the clankety, clankety, clankety which is customarily done here with the iron-fisted discussion of the statute. That's true, I didn't. I refuse to go any further. (T.2387)

The government's theory was that the defendants were aiders and abettors; the trial court instructed the jury that it could convict on a finding of aiding and abetting; its failure to define that term was reversible error. *United States* v. *Terrell,* 474 F.2d 872 (2d Cir. 1973); *United States* v. *Byrd,* 352 F.2d 570 (2d Cir. 1965); *United States* v. *Garguilo,* 310 F.2d 249 (2d Cir. 1962).

In each of these cases, some instruction defining aiding and abetting was given to the jury. Yet, in each, because of the closeness of the issues, this Court held the definitions given to have been inadequate and reversed. The result is

a fortiori here where aiding and abetting was not defined at all.

Thus, the trial court refused even to read the aiding and abetting statute under which Natelli and Scansaroli were charged. This would not have been sufficient under *United States* v. *Byrd*, *supra*, 352 F.2d at 576, but it might have been better than nothing.* And the jury simply was not told by the court what it had to find in order to convict these two men as aiders and abettors. In a close case, as this one obviously was, the trial court's failure was fatal.

In *Garguilo* and *Terrell*, this Court reversed convictions because the trial court's usual instructions concerning aiding and abetting, characterized in *Garguilo* as "adequate, indeed excellent in the usual trial," 310 F.2d at 254, were insufficient in a close case:

> [W]e would still be disposed to direct a new trial even though the evidence was sufficient. The closeness of the issue against [the defendant] imposed an obligation on the trial judge to instruct the jury with extreme precision, as he realized, and on us to review the charge with what, in a less doubtful case, would be undue meticulousness. See Glasser v. United States, 315 U.S. 60, 67, 62 S.Ct. 457, 86 L.Ed. 680 (1942); United States v. Persico, 305 F.2d 534, 536 (2 Cir. 1962).

United States v. *Garguilo*, *supra*, 310 F.2d at 254; *accord*, *United States* v. *Terrell*, *supra*, 474 F.2d at 876.

We do not claim that an accountant can never be guilty of aiding and abetting a corrupt client in issuing false financial statements. However, given the nature of the circumstances—that the financial statements are the company's and not the accountants' and that the responsibility

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* The Government submitted a two page request to charge on this issue (Gov't Request No. 10, A.152-53), but sat silent when exception was taken by the defense to the court's omission.

of the independent auditor for unaudited statements must be distinguished from his role in an audit (unexplained to the jury below)—it was crucial for the court to have charged the jury with precision on the concept of aiding and abetting.

Even in a relatively simple case, prejudicial confusion could result in the jury's mind from the omission of an aiding and abetting definition. In this case, replete with complex accounting issues and a bewildering quantity of technical and documentary evidence, the jury could have easily misunderstood what was needed to convict Scansaroli. And since the issue of Scansaroli's participation was close at best, the impact of such confusion was dramatically magnified by the failure to make any effort to define terms that are foreign to laymen. The conviction should be reversed.

CONCLUSION

For the reasons stated above, we respectfully submit that the conviction of defendant Joseph Scansaroli should be reversed.

Respectfully submitted,

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Dated: New York, New York
March 3, 1975.

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Due and timely service of TWO copies
of the within BRIEF is hereby
admitted this 3RD day of APRIL 1975

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Attorney for APPELLEE